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October 6, 2008

VIA Electronic Submission

Ms. Marlene H. Dortch
Secretary
Federal Communications Commission
445 12th Street S.W.
Washington, D.C. 20554

Re: Developing a Unified Intercarrier Compensation Regime, CC Docket No. 01-92; Federal-State Joint Board on Universal Service, CC Docket No. 96-45; Intercarrier Compensation for ISP-Bound Traffic, WC Docket No. 99-68

Dear Ms. Dortch:

On behalf of Pac-West Telecomm, Inc., Dr. Lee Selwyn and the undersigned met with Nicholas Alexander of Commissioner McDowell's office, Greg Orlando of Commissioner Tate's office, Scott Deutchman of Commission Copp's office, Scott Bergman of Commissioner Adelstien's office, and Randy Clarke and other staff members of the Marcus Maher, Randy Clarke, Mathew Warner, Claude Aiken, and Nicholas Degani of the Wireline Competition Bureau on October 6, 2008. At these meetings, Pac-West discussed issues related to intercarrier compensation, as set forth in written presentation materials, a copy of which is attached hereto.

Sincerely,

James M. Tobin

Attachment

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Comprehensive ICC Reform through Cost-Based Rates

Pac-West Telecomm, Inc.

Jim Tobin, General Regulatory Counsel
Dr. Lee Selwyn, President - Economics and Technology, Inc.

Comprehensive ICC Reform

Any comprehensive reform of Intercarrier Compensation must be premised upon the adoption of cost-based rates

<u>Cost-Based Transport and Termination Rates:</u>

- Are essential in order to avoid arbitrage and regulatory gaming both by ILECs and by CLECs Justifiable
- Are currently in existence through state public utility commissions rate making proceedings
- Are required by §252(d)(2)
- Do not depend on cross-subsidization from originating access or other support mechanisms

Importance of a Properly Set Call Termination Charge

Properly set call termination charges should be:

- Established on the basis of forward looking economic costs
- Applicable to all types of traffic

Properly set call termination charges would:

- Permit and encourage all carriers to compete on an equal basis
- Allow the competitive marketplace to determine ultimate market outcome

Importance of a Properly Set Call Termination Charge

Cost-based ICC rates provide the best means for assuring efficient and competitively-neutral market outcomes.

Policy	Consequence
Set call termination reciprocal compensation rate above cost	Providers seek out customers with high inward calling demand (e.g., ISPs); large traffic imbalance of inbound minutes
Set call termination reciprocal compensation rate below cost (e.g., at $0.0007 or bill-and-keep)	Providers seek out customers with high outward calling demand (e.g., call centers, telemarketers); large traffic imbalance of outbound minutes
Set call termination reciprocal compensation rate at cost (TELRIC)	Providers make economically efficient choices as to the types of customers they serve and the types of technologies they support

Cost-Based Rates

- The $0.0007 “rate cap” specified in the *ISP Remand Order* and now embraced by numerous parties is well below costs

- The $0.0007 rate was just one element in negotiated interconnection agreements that, like any negotiation, necessarily involved various tradeoffs in other areas, and has no precedential effect when taken in isolation

- Most importantly, the $0.0007 rate is well below cost, as cost was determined in numerous contested state PUC UNE proceedings and sec. 252(c) arbitrations

ILEC Cost-Based Reciprocal Compensation Rates vs. ISP-bound Reciprocal Compensation Rate of $0.0007

State	ILEC	Rate Per MOU	% Higher than ISP rate (assumes 20 minute call length)
AZ	Qwest	$0.0015200	**217%**
CA	at&t	$0.0030830	**440%**
CA	Verizon	$0.0019280	**275%**
CO	Qwest	$0.0026590	**380%**
FL	at&t	$0.0008981	**128%**
FL	Verizon	$0.0029030	**415%**
NY	Verizon	$0.0039620	**566%**
NV	Embarq	$0.0039930	**570%**
NV	Verizon	$0.0101419	**1449%**
NV	at&t	$0.0040320	**576%**
OR	Qwest	$0.0036700	**524%**
OR	Verizon	$0.0036700	**524%**
PA	Verizon - E	$0.0011016	**157%**
PA	Verizon - W	$0.0030000	**429%**
TX	at&t	$0.0011773	**168%**
UT	Qwest	$0.0026060	**372%**
WA	Qwest	$0.0026280	**375%**
WA	Verizon	$0.0070160	**1002%**

Applying the FCC TELRIC methodology, State PUCs have established TELRIC-based call termination rates, which are almost uniformly in excess of $.0007 on a State-specific and carrier specific basis.

Cost Based Rates Should be Uniform…

- As to functionality
  - Call termination rates should be the same for local calls, interexchange calls, ISP bound calls,
- As to jurisdiction
  - Same for intrastate and interstate traffic
- But Not As To Service Provider
- But Not Across All States
  - States are and should remain responsible for establishing cost based, carrier specific ICC rates

Advocates of $.0007 Support Cross Subsidization of Terminating Access

- **In its September 19, 2008 *ex parte*, Verizon admits that:** "Section 252(d)(2) sets a standard for assessing rates for §251(b)(5) traffic: such rates must reflect a 'reasonable approximation of the additional costs of terminating ... calls' subject to § 251(b)(5)."

- **But Verizon goes on to suggest that:** ... exercising its rulemaking authority, the Commission can find that its national default rate ... is also a 'reasonable approximation of th[os]e additional costs,' ... particularly in light of the opportunities that service providers have under Verizon's proposal to recover additional amounts from retail customers and from a Replacement Mechanism.

- Verizon is asking the Commission to use the Replacement Mechanism and other payments imposed on retail end users to cross-subsidize Verizon's call termination obligations to other LECs

- There is no reasonable way to read §252(d)(2) as authorizing the Commission to sanction such cross-subsidization

Advocates of $.0007 Support Cross Subsidization of Terminating Access

- In its September 19, 2008 *ex parte*, Verizon admits that:" … [CLEC business] opportunities that depend upon high, one-way volumes of traffic — such as … serving ISPs exclusively — become uneconomical when the per minute rate for such calls is $0.0007 or less." [p. 32]

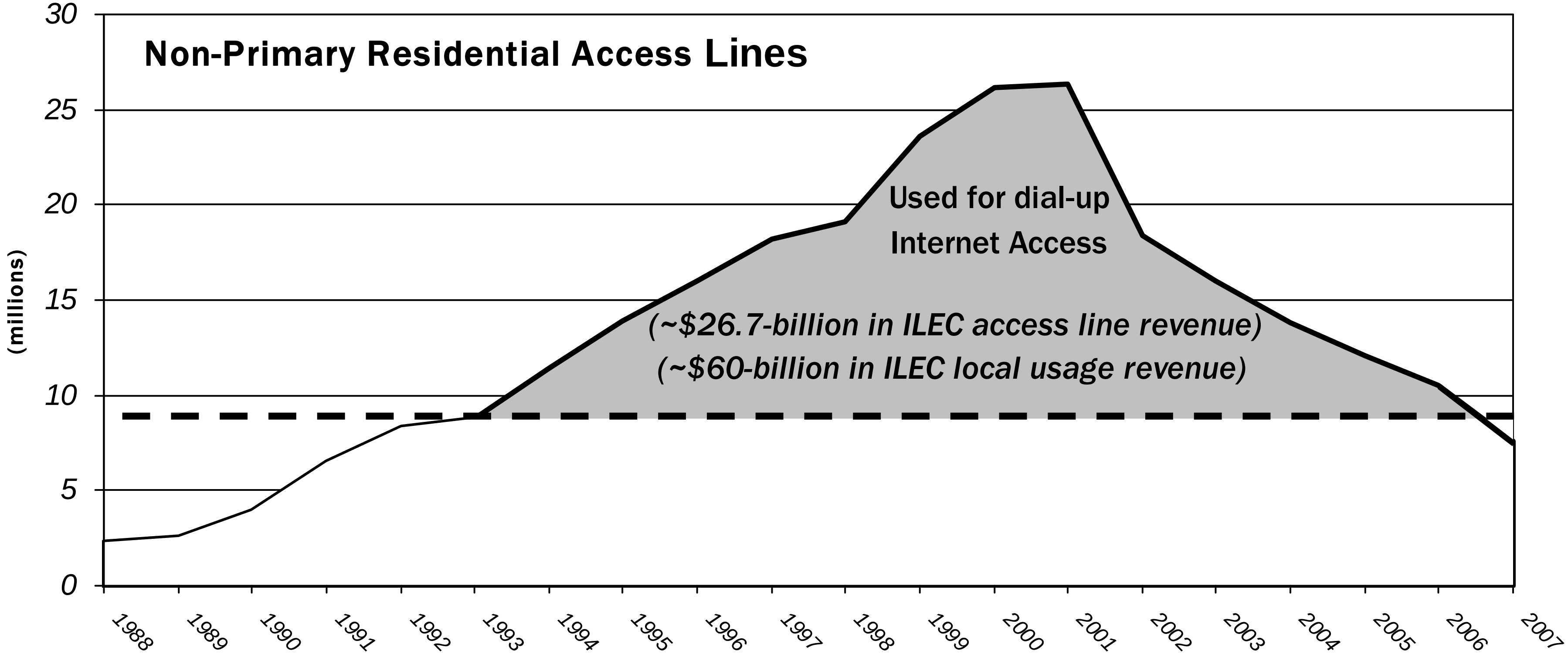
- There is nothing immoral or unethical in pursuing legitimate business models that involve specialization in serving certain types of customers or traffic

- ILECs have *never* shown any serious interest in providing inbound dial-up services to ISPs – the vast majority of that demand was served by CLECs specializing in supporting "upon high, one-way volumes of traffic."

- Verizon's demeaning and dismissive pejoratives about "high, one-way volumes of traffic" are not a valid basis for the Commission to allow Verizon and other ILECs to escape their §252(d)(2) obligation to pay cost-based call termination rates for ISP and all other traffic handed off to CLECs.

Dial-up Internet use is Extraordinarily Profitable for the ILECs

- Rhetoric aside, use of dial-up Internet access has been – and continues to be – an enormous source of ILEC revenue
- At its peak in 2001, some 26.3-million US households had installed additional residential exchange service lines, at least 18-million of which were being used mainly for Internet access



Dial-up Internet use is Extraordinarily Profitable for the ILECs

- If we *conservatively* assume that ILEC revenue was 1-cent per minute, during the 1993-2007 period ILECs collected roughly ***$60-billion*** from their end user customers for originating dial-up ISP-bound traffic, mostly terminated by other carriers.

	Dial-up Internet Users	Average Daily Minutes per Dial-up Internet User	Total Annual Minutes of Dial-up Internet Use
AOL (2001)	33-million (Note 1)	61 minutes (Note 2)	734.7-billion
Other Dial-up ISP (2001)	18.9-million (Note 3)	30.5 minutes (Note 4)	207.0-billion
Total 2001			941.7-billion
Total 1993-2007			6.023-trillion (Note 5)

Dial-up Internet use is Extraordinarily Profitable for the ILECs

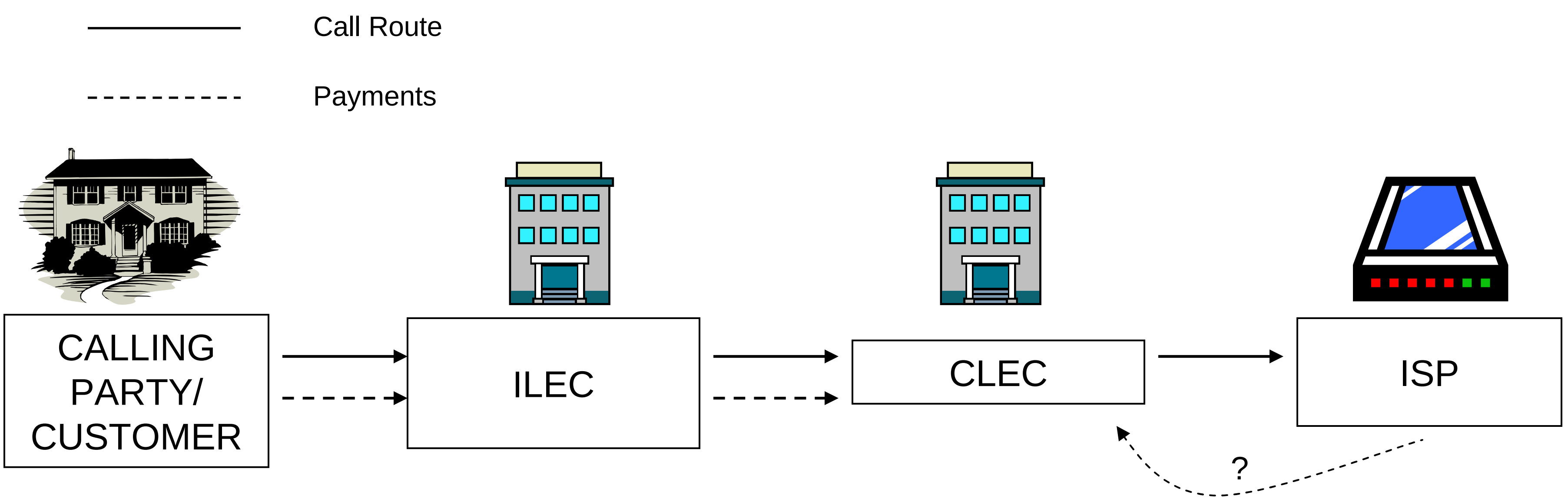
- Dial-Up Internet Access calls are rated and charged to the end user *as sent paid* local calls, and produce massive amounts of local usage revenue for the originating LEC

- Even when local usage is provided on a so-called "flat rate" or "unlimited" basis, there is still a monthly "local usage charge" that the customer must pay in order to use dial-up Internet access services

- In addition to realizing some <u>$26.7-billion</u> in second line monthly access revenues, between 1993 and 2007, ILECs collected roughly <u>*$60-billion*</u> in local usage charges associated with dial-up calls to ISPs, most of which were handed off to CLECs for termination at below-cost termination charges

- There can be no rational economic or policy basis for allowing the originating LEC to escape its obligation to compensate the terminating LEC for the full cost of termination

ILEC Revenues From Local Dial-up Internet Access Usage



Pays Local Usage Charge to ILEC

ILEC Pays Termination Charge to the CLEC Capped at $0.0007

Is Being Told to Recover Costs of Termination From ISP Customers

Pac-West and Dial-Up Users

- Virtually all dial-up ISP-bound calls have been originated by ILEC customers and handed off to CLECs for termination to ISPs
- ILECs have made little or no serious effort to attract ISP business
- Which is hardly surprising, given that ILECs can terminate ISP-bound calls to CLECs at $0.0007, i.e., at around a quarter to a third of what it would cost them to do it themselves
- Adoption of some sort of “bill-and-keep” scheme would give ILECs even less incentive to compete for ISP business, since they will be able to terminate ISP-bound calls to CLECs for free.
- Dial-up remains profitable for ILECs
- Pac-West’s ability to provide dial-up Internet access to ISPs is not economically sustainable at the $0.0007 rate

Pac-West and Dial-Up Users

<u>Dial-Up is a key alternative for Low-Income and Rural Customers</u>

- Pac-West continues to fill that role by providing wholesale services to Internet Service Providers (ISPs)
- Without cost-based ICC, costs to ISPs will increase which in turn will increase costs to those in need of an alternative to broadband

<u>Dial-Up is declining but needed</u>

Dial-Up access is relied on disproportionately by poorer citizens and minorities*

- 29% of dial-up users live in households with annual incomes of less than $30,000
- 43 % of dial-up users are age 50 or older
- 30% of dial-up users live in rural areas

**Study by the Pew Internet & American Life Project (as of June 2007)*

APPENDIX

Calculation of ILEC exchange access and usage revenue from Dial-up Internet use (1993-2007)

NOTES: Dial-up Internet use is Extraordinarily Profitable for the ILECs

- Estimation of total ILEC Non-Primary Residential Access Line Revenue attributable to dial-up Internet use for the period 1993-2007
- Use FCC Non-Primary line data, using 1993 as a pre-Internet benchmark
  - Calculate the excess of Non-Primary lines over the pre-Internet benchmark for the period
    - (Data for 2007 estimates the excess only for the portion of the year when an excess over the benchmark existed)
  - Multiply the result by a conservative estimate of $20 in access line revenue per line per month
  - Multiply the result by 12 to annualize the revenue

	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Non-Primary Lines	8.8	11.4	13.9	16	18.2	19.1	23.6	26.2	26.3	18.4	16	13.8	12.1	10.5	7.6
Benchmark	8.8	8.8	8.8	8.8	8.8	8.8	8.8	8.8	8.8	8.8	8.8	8.8	8.8	8.8	8.8
Non-Primary Lines in excess of 1993 benchmark		2.6	5.1	7.2	9.4	10.3	14.8	17.4	17.5	9.6	7.2	5	3.3	1.7	0.43

Total 1993-2007 Lines in Excess of Benchmark	111.53
Revenue per line per month	$20.00
Total Annualized Revenue	$26,766.67

NOTES: Dial-up Internet use is Extraordinarily Profitable for the ILECs

- Note 1: “AOL's Formula: Does It Add Up?,” *Fortune*, Stephanie N. Mehta, 2/4/02, available at http://money.cnn.com/magazines/fortune/fortune_archive/2002/02/04/317480/index.htm

- Note 2: AOL 2001 10-K Annual Report filed March 25, 2002

- Note 3: Total 2001 ISP Dial-up lines (51.9-million) net of 33-milllion AOL lines. Jupiter Research

- Note 4: Conservative assumption of half the use of AOL subscribers

- Note 5: FCC *Trends in Telephone Service*, August 2008

NOTES: Dial-up Internet use is Extraordinarily Profitable for the ILECs

- Estimation of total dial-up minutes of use for the period 1993-2007
- Calculate the percentage of dial-up use in 2001 relative to the period 1993-2007.
  - Use FCC Non-Primary line data, using 1993 as a pre-Internet benchmark
  - Calculate the excess of Non-Primary lines over the pre-Internet benchmark for the period
    - (Data for 2007 estimates the excess only for the portion of the year when an excess over the benchmark existed)
  - Calculate the excess of Non-Primary lines over the pre-Internet benchmark for 2001
  - Calculate 2001 as a percentage of the total period

	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Non-Primary Lines	8.8	11.4	13.9	16	18.2	19.1	23.6	26.2	26.3	18.4	16	13.8	12.1	10.5	7.6
Benchmark	8.8	8.8	8.8	8.8	8.8	8.8	8.8	8.8	8.8	8.8	8.8	8.8	8.8	8.8	8.8
Non-Primary Lines in excess of 1993 benchmark		2.6	5.1	7.2	9.4	10.3	14.8	17.4	17.5	9.6	7.2	5	3.3	1.7	0.43
										Total 1993-2007 Lines in Excess of Benchmark					111.5
											Total 2001 Lines in Excess of Benchmark				17.5
													2001 percentage		0.15691

- Calculate the total dial-up usage for 2001
  - Use AOL data for AOL users
  - Use conservative estimate of use (50% of AOL reported use) for the remaining dial-up users
  - Gross up 2001 data for the period 1993-2007 using "2001 percentage" calculated above

734,745,000,000	AOL 2001 minutes (33-million subs, 61 minutes, 365 days)
210,404,250,000	Other ISP 2001 minutes (18.9-million subs, 30.5 mins, 365 days)
945,149,250,000	Total 2001 Minutes (sum)
0.156912	2001 percentage of total 1993-2007 period
6,023,451,172,619	Total period minutes (2001 minutes / 2001 percentage)